

alone businesses.<sup>47/</sup> The revenue they generate by selling national time in programming made available to affiliated stations is not sufficient to cover the costs of acquiring or producing that programming.<sup>48/</sup> The source of a network company's profit on the huge sums it must invest to obtain original and "event" programming is its owned and operated stations. Thus, the profits generated by the owned stations provide the networks with both the ability and the incentive to acquire and produce high quality, popular programming.

Limiting the number of stations a network can own has the effect of limiting its ability or willingness to invest in programming for free, over-the-air television. This ultimately harms viewers and local stations, and threatens other major sectors of the television industry, such as program producers and syndicators who rely on the networks as the primary support for original entertainment programming.

As Dr. Katz indicates:

the national cap limits network ownership of stations, and ownership is the institutional arrangement that most fully aligns the economic incentives of a network and a station broadcasting its programming. The increased profits derived from owned and operated stations are an important factor in determining a networks[']s willingness and ability to bid for costly event programming such as the broadcast rights to National Football League games, the Olympics, and theatrical movies. Station ownership also affects the networks' incentives to invest in programming developed solely for television, such as comedies and dramas. By limiting the extent to which networks can own stations, the national multiple ownership rule thus reduces television networks' incentives and abilities to promote and compete for high-quality, high cost programming dedicated to [free, over-the-air television].<sup>49/</sup>

The consequence of economic distortions caused by the national ownership cap is to push the companies that own broadcast networks to invest in alternative means of distributing programming content, such as cable television and the Internet. The broadcast networks distribute their

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<sup>47/</sup> See Peter Chernin, Testimony before the House Subcommittee on Telecommunications, Trade, and Consumer Protection, September 15, 1999 at 11.

<sup>48/</sup> See Katz at 45-47.

programming through free, over-the-air television stations, but their parent companies have significant investments in cable and Internet properties.<sup>50/</sup> While these investments may represent a wise use of resources, the balance between investments in broadcast programming and cable or Internet content should not be based on the arbitrary constraints imposed by the national ownership rules.<sup>51/</sup> To the extent that networks choose to develop alternative media outlets in lieu of over-the-air programming because they cannot recapture their investments in broadcast shows, the rules harm broadcast viewers by discouraging production of high-quality programming for free television.<sup>52/</sup>

By forcing the networks to rely on affiliates for the distribution of programming to at least 65 percent of the nation's households, the current rules require the networks to bear the full burden of investments in broadcast programming while limiting their ability to recover these investments. In light of current market conditions, the ownership cap is an unwarranted restraint on the ability of the broadcast television industry to compete against the growing number of outlets for video programming. The public interest plainly requires elimination of the national ownership rule's inefficient and distorting effects free over-the-air television.

### **C. The Rule Does Not Promote Public Interest Goals**

In theory, the national broadcast ownership rule might create public interest benefits that outweigh its documented costs. However, as Dr. Katz's study establishes, there is no evidence that the national broadcast ownership rule has achieved, or is necessary to promote, any public interest goal that has been advanced to justify it.

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<sup>49/</sup> Id. at 56.

<sup>50/</sup> Id. at 48.

<sup>51/</sup> Id. at 51.

<sup>52/</sup> The fact that the companies that own the networks may remain profitable despite the ownership cap is irrelevant. The point is not that the networks will go out of business if they are denied access to the revenue stream available through ownership of additional stations, but that

First, the rule does not promote competition. Fundamentally, competition for viewers takes place at the local level. Policy makers, including the Commission, have long ago concluded that the national cap does nothing to promote or protect local competition. For example, the U.S. Department of Justice filed comments in a 1983 Commission proceeding in which the Department stated that eliminating the national multiple ownership limits would “raise little risk of adverse competitive effects in any market.”<sup>53/</sup> The Commission itself reached a similar conclusion in its 1984 Report and Order.<sup>54/</sup>

Indeed, relaxing the national ownership cap might actually increase competition in several dimensions. The greater coordination efficiencies that increased network ownership would bring about would increase the networks’ incentives to improve their program offerings, thus strengthening competition for viewers and ultimately advertisers. In the same way, this increased coordination would also intensify competition in the markets for programming and creative talent.

Moreover, as Dr. Katz concludes, any argument that the national broadcast ownership limit protects the preserved economic interest of network affiliates is fundamentally flawed as a factual matter, and confuses the affiliates’ private interest with the public interest.<sup>55/</sup>

Second, the national broadcast ownership rule does not meaningfully promote diversity. Again, as Dr. Katz convincingly establishes, the rule has had no direct effect on diversity, and relaxation of the rule could in fact promote increases in the provision of news and public affairs

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the networks will have inadequate incentives to invest in high-quality programming. See id. at 59.

<sup>53/</sup> In the Matter of Amendment of Section 73.3555 [formerly Sections 73.35, 73.240, and 73.636] of the Commission’s Rules Relating to Multiple Ownership of AM, FM, and Television Broadcast Stations, Gen. Docket No.83-1009, Report and Order, 100 FCC 2d 17 (released August 3, 1984) at ¶ 65.

<sup>54/</sup> Id. at ¶ 108.

<sup>55/</sup> Katz at 62-67.

programming.<sup>56/</sup> The Commission has distinguished at least three concepts of diversity -- outlet, source and viewpoint. However, what ultimately matters to citizens is the degree of viewpoint diversity. As Dr. Katz notes, there is no evidence that disparate station ownership on the national level has any effect on diversity of viewpoint on the local level. Because the national cap has no effect on the number of local stations that can be received in any given local market, the cap has no effect on source or outlet diversity in any event.

Defenders of the rule have asserted that what is shown on a local station in one city can affect viewers in another city. This line of argument holds that a viewpoint first expressed in one area will later spread to other cities as the story is picked up by other media. However, the Commission rejected this argument in 1984 in this context on the grounds that: (a) group owners “do not impose monolithic viewpoints on local media outlets”; (b) there are a huge number of “idea sources” nationwide; and (c) group ownership has “offsetting advantages”.<sup>57/</sup>

Third, the rule does not promote minority ownership. Dr. Katz demonstrates in his report that there is no factual support for the theory advanced that past or current national ownership caps have resulted in any increase in minority ownership or that removing the cap will harm minority ownership.<sup>58/</sup>

Finally, the rule does not promote localism. Again, there is no evidence that non-local owners failed to serve local needs. In fact, the Fox local stations present a considerable amount of local programming.<sup>59/</sup> Indeed, the vast majority of stations already are operated by group owners. Further, since most affiliates are already run by group owners, relaxing the national cap would not significantly reduce the total number of single-station affiliate owners. Lastly, to the extent that

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<sup>56/</sup> Id. at 67-72.

<sup>57/</sup> Id. at 61-62.

<sup>58/</sup> Id. at 72-77.

localism is important to viewers, there are strong market incentives for broadcasters to serve local needs, regardless of the number of stations they own.<sup>60/</sup> The vast majority of local programming currently available to viewers is produced by local stations, not by cable or DBS.

### **III. The Commission's Recent Orders Relaxing the Broadcast Duopoly and Cable Horizontal Ownership Rules Reinforce the Lack of Foundation for Continued Retention of the National Limits on Broadcast Ownership**

Within the last few months, the Commission has issued orders revising both its rule limiting the number of television stations that can be owned by a single entity in the same market and its regulations restricting horizontal ownership of cable systems.<sup>61/</sup> In these orders, the Commission confronted the same overarching issue it faces in connection with the national limits on broadcast station ownership: whether retention of an ownership restriction makes sense in light of increased competition and changed market conditions. In both cases, the Commission concluded that competitive developments warranted changes to the ownership restrictions at issue. In several respects, the analysis and reasoning employed by the Commission in the duopoly and cable horizontal proceedings demonstrate the absence of any empirical evidence or sound analytical basis for retention of the national limits on television station ownership.

#### **A. The Revisions to the Broadcast Duopoly Rules Underscore the Lack of Foundation for Continued Retention of the National Ownership Limits**

In the Local Television Ownership Review Order the Commission itself acknowledged that national station ownership limits do little to promote diversity. The reason is simple: the diversity

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<sup>59/</sup> See Fox Comments at 15-18.

<sup>60/</sup> Id. at 78-81.

<sup>61/</sup> In the Matter of Review of the Commission's Regulations Governing Television Broadcasting, Television Satellite Stations Review of Policy and Rules, FCC 99-209, MM Docket No. 91-221, MM Docket No. 87-8, 11 FCC Rcd 21655 (rel. August 6, 1999) ("Local Television Ownership Review Order"); In the Matter of Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992, Horizontal Ownership

interest is only implicated at the local level. In attempting to “foster . . . diversity goals,” the Commission aims to “maximize the available independent viewpoints in a given local market.”<sup>62/</sup> Thus, the Commission acknowledged in the Local Television Ownership Review Order that the “concern for ensuring diversity is most pressing at the local level.”<sup>63/</sup>

It would be difficult for the Commission to conclude otherwise, particularly when considering its previous statements and actions. Dating back to 1984, the Commission has voiced substantial doubts regarding the necessity and utility of national limits on broadcast ownership in promoting competition and diversity.<sup>64/</sup> More recently, in 1995, the Commission observed that “the national ownership rules . . . may not be essential to achieving diversity.”<sup>65/</sup> The Commission noted in 1996 that “our concern with diversity is most acute with respect to local ownership issues.”<sup>66/</sup> Likewise, with respect to competition, the Commission has stated that:

Relaxing the national ownership limits will not by itself increase or decrease the number of separately owned broadcast stations in the video program delivery market. This is because, as discussed earlier, the video program delivery market is a local market. So, as long as a company is allowed to own only one broadcast television station in a local market, relaxing the national ownership limits will have no affect on the concentration of these local markets.<sup>67/</sup>

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Limits, MM Docket No. 92-264, Report and Order, FCC 99-289 (rel. October 20, 1999) (“Cable Horizontal Ownership Review Order”).

<sup>62/</sup> Local Television Ownership Review Order at ¶ 24.

<sup>63/</sup> Local Television Ownership Review Order at ¶ 19.

<sup>64/</sup> See Fox Comments at 5-9.

<sup>65/</sup> In the Matter of Review of the Commission’s Regulations Governing Television Broadcasting; Television Satellite Stations Review of Policy and Rules, MM Docket Nos. 91-221 and 87-8, Further Notice of Proposed Rulemaking, 10 FCC Rcd 3524, 3564, ¶ 96 (1995) (“Broadcast Regulation Review FNPRM”).

<sup>66/</sup> In the Matter of Review of the Commission’s Regulations Governing Television Broadcasting; Television Satellite Stations Review of Policy and Rules, MM Docket No. 91-221, MM Docket No. 87-8, Second Notice of Proposed Rulemaking, 11 FCC Rcd 21655, 21657 (1996).

<sup>67/</sup> Broadcast Regulation Review FNPRM, 10 FCC Rcd at 3560, ¶ 83.

For decades, the Commission has both permitted and promoted the national network structure that has been the hallmark of broadcast television, even though the result is that hundreds of stations across the country broadcast the identical schedule of network programs.<sup>68/</sup> As the Commission itself has observed:

Television and competing outlets are viewed locally, and we question whether an increase in concentration nationally affects diversity on the local level. In this regard, also, many stations are affiliated with a network. As a result, these stations, even though not commonly owned, air the identical programming for a large portion of the broadcast day irrespective of our national ownership limits.<sup>69/</sup>

The Commission correctly does not regard the mere ability of a single entity (*i.e.*, a national network) to propagate the same “message” in many different markets around the country to implicate diversity concerns. By the same token, the ownership by one entity of a television station in each of many different markets around the country also should not raise diversity concerns -- even assuming *arguendo* that that entity would convey the same “message” uniformly in every one of those different markets. In fact, as Fox showed in its initial comments, the historical record demonstrates that group ownership of broadcast stations at the local level actually promotes viewpoint diversity, since group owners experience scale economies and shared costs that help fuel new investment in local programming.<sup>70/</sup> Indeed, since one of the principal motivations driving acquisition of local stations is

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<sup>68/</sup> See Stanley M. Besen et al., *Misregulating Television* 1-2, 4-19 (1984) (suggesting that FCC regulations have permitted the national network structure and even promoted it); see also Implementation of the Cable Television Consumer Protection and Competition Act of 1992 Broadcast Signal Carriage Issues, MM Docket No. 92-259, Order, 9 FCC Rcd 6723, 6747 at ¶ 113 (1994) (indicating that the Commission’s enforcement of nonduplication rights is designed, in part, to promote the ability of the networks to distribute their programming).

<sup>69/</sup> Broadcast Regulations Notice, 10 FCC Rcd at 3565, ¶ 96.

<sup>70/</sup> Fox Comments at 15-19; Joint Reply Comments of Fox Television Stations, Inc., and USA Broadcasting, In the Matter of 1998 Biennial Regulatory Review -- Review of the Commission’s Broadcast Ownership Rules and Other Rules Adopted Pursuant to Section 202 of the Telecommunications Act of 1996, MM Docket No. 98-35 (filed August 21, 1998) (“Fox Reply Comments”) at 8-12. In an *ex parte* submission filed earlier this year, NTIA asserted that raising the national ownership cap would somehow reduce local programming and viewpoint diversity.

the opportunity to garner new revenue from the sale of local advertising, group owners have a powerful interest in ensuring that their programming in local markets is responsive to community needs and interests.<sup>71/</sup>

While the Commission's interests in promoting broadcast diversity and competition are implicated most directly and significantly at the local level, it nonetheless opted to relax the duopoly rule and allow ownership by a single entity of more than one television station in the same market. This decision was predicated upon the substantial evidence demonstrating the increasing level of competition faced by broadcast stations.<sup>72/</sup> As Chairman Kennard observed in his statement accompanying the Commission's relaxation of the duopoly rule:

[W]e are adopting commonsense rules that recognize the dramatic changes that the media marketplace has undergone since our broadcast ownership rules were adopted 30 years ago. Back then, there were three broadcast networks; cable was still a novelty; and interactive TV meant yelling at your kids to turn it down. Now cable systems serve almost 65 million TV households; other multichannel video programmers -- such as Direct Broadcast Satellite -- offer hundreds of channels to viewers; since 1970, the number of radio and television stations has increased by more than 85 percent; and people are watching

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See Letter of February 12, 1999, from Larry Irving, National Telecommunications and Information Administration, to William E. Kennard, Chairman, Federal Communications Commission, at 6-7 ("NTIA Letter"). This contention is demonstrably incorrect.

<sup>71/</sup> Thus, NTIA's suggestion that group owners have "few incentives to produce and air local programming or to target specific community needs," see NTIA Letter at 7, lacks both economic and empirical support. See Katz at 67-72. In fact, independent stations appear to spend less on locally-generated programming than network affiliates. See In the Matter of Review of the Commission's Rules Governing Television Broadcasting; Television Satellite Stations -- Review of Policy and Rules, MM Docket Nos. 91-221 and 87-8, Further Notice of Proposed Rulemaking, 10 FCC Rcd 3524, 3566 n. 124 (1995) ("Broadcast Review FNPRM") ("information currently available to us suggests that affiliates spend almost four times the amount spent on news by independents"). The Commission has noted that ownership of a larger number of stations logically results in efficiencies that allow a larger allocation of resources to news. Broadcast Review FNPRM, 10 FCC Rcd at 3566 n. 125 ("Intuitively, we believe that any impact [of larger stations groups] would be positive. Ownership of more stations would, we believe, enhance the resources that a network or group owner could devote to its news operations.")

<sup>72/</sup> Local Television Ownership Review Order at ¶¶ 28-29; id. at ¶ 33 ("evidence justifies some relaxation of our local television ownership rules, as it suggests that consumers and advertisers may have more viable alternatives to broadcast stations than they once had").

everything from hip-replacement surgery to the local weather on their PCs linked to the Internet. As we cross over into the next millennium, we are clearly entering a new media age.

In such an age, we need to provide broadcasters with flexibility to seize opportunities and compete in the increasingly dynamic media marketplace. These items will not only help them compete with the growing number of alternative media. They will also help preserve free local broadcast service.<sup>73/</sup>

Having found that the evidence of increased competition and changed market conditions supports relaxation of ownership restrictions at the local level, where the competition and diversity interests are most compelling, it follows that those same market conditions warrant even greater relaxation of ownership restrictions at the national level, where the Commission has acknowledged that those interests are implicated less substantially. In fact, it is difficult to imagine that the Commission could reach a decision to the contrary that could withstand judicial scrutiny.<sup>74/</sup>

This conclusion is buttressed by the mechanics of the modifications to the duopoly rule adopted by the Commission. Not only did the Commission relax the rule by shrinking its geographic scope from the Grade B contour to Designated Market Areas (DMAs),<sup>75/</sup> it took the more significant step of expressly permitting duopolies within the same DMA under certain circumstances.<sup>76/</sup> Specifically, the Commission will allow broadcast duopolies within the same local market so long as eight independent broadcast stations remain within that DMA and only one of the commonly-owned stations is ranked within the top four of that local market. Likewise, the Commission decided to count a duopolist's audience in a particular local market only once, for purposes of determining compliance with the national cap.<sup>77/</sup> Thus, the Commission again recognized that only local market

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<sup>73/</sup> Id. (separate statement of Chairman William Kennard, August 5, 1999).

<sup>74/</sup> See supra Section II.

<sup>75/</sup> Local Television Ownership Review Order at ¶¶ 47-53.

<sup>76/</sup> Id. at ¶¶ 64-70.

<sup>77/</sup> In the Matter of Review of the Commission's Regulations Governing Television Broadcasting, Television Satellite Stations Review of Policy and Rules, MM Docket No. 96-221,

effects need be considered when assessing the utility of relaxing a broadcast ownership restriction.<sup>78/</sup> Since the Commission already has acknowledged that there are no local market effects associated with relaxing the national limits on broadcast ownership,<sup>79/</sup> it follows that those restrictions should be eliminated.

The rationale for relaxing the duopoly rule effectively evaporates any remaining analytical basis for retaining national limits on broadcast ownership. If competition and diversity are not undermined by having a single entity own two broadcast stations in Los Angeles, then the Commission would be hard-pressed to justify why it should preclude that same company from owning one station in Los Angeles and one station in Houston, simply because the addition of the Houston station puts the company over an arbitrary percentage of total TV households. Clearly, whatever impact on competition and diversity arises in these examples is more acute in the case of multiple ownership in Los Angeles, than in the case of single station ownership in Los Angeles and

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MM Docket No. 91-221, MM Docket No. 87-8, Report and Order, FCC 99-208 (rel. August 6, 1999) at ¶ 1.

<sup>78/</sup> Katz at 69-70.

<sup>79/</sup> See In the Matter of Amendment of Section 73.555 of the Commission's Rules Relating to Multiple Ownership of AM, FM and Television Broadcast Stations, Gen. Docket No. 83-1009, Report and Order, FCC 84-350, 100 FCC 2d 17, 38-42, ¶¶ 65-73 (1984) (noting Department of Justice's conclusion that "elimination of the Seven Station Rules will raise little risk of adverse competitive effects in any market"). In fact, it is more likely that there would be efficiency gains in terms of news gathering, editorializing, public affairs programming, the development of independent programming, superior management capability, and economies of scale. See id. at 44-45, ¶ 82. Fears of network collusion leading to potential anticompetitive conduct have proven unfounded in the markets where networks own stations, including the top three. See In the matter of Amendment of Section 73.555 of the Commission's Rules Relating to Multiple Ownership of AM, FM and Television Broadcast Stations, Gen. Docket No. 83-1009, Memorandum Opinion and Order, 100 FCC 2d 17 at ¶ 28 (1994). Any net impact is likely to be positive because of the shared resources between network and affiliate. See In the Matter of Review of the Commission's Regulations Governing Television Broadcasting, Television Satellite Stations Review of Policy and Rules, MM Docket Nos. 91-221, 87-8, Further Notice of Proposed Rulemaking, 10 FCC Rcd 3524, 3566 n.125 (1995).

Houston. Paradoxically and without justification, the Commission's current regulatory framework permits the former but prohibits the latter arrangement.

**B. The Modifications to the Cable Horizontal Ownership Rules Reinforce the Need to Eliminate or Dramatically Modify the National Broadcast Ownership Limits**

The Commission's Order modifying the cable television system horizontal ownership rules, released last month, also underscores both the need to alter the national limits on broadcast station ownership and the difficulty the Commission will confront in legally defending any decision to leave the cap unchanged under applicable judicial standards. Previously, the Commission's cable horizontal ownership rules limited the national reach of a single multi-system cable operator (MSO) to 30% of the total homes passed nationwide by all cable systems.<sup>80/</sup> As a result of the modifications adopted in the Cable Horizontal Ownership Order, a single cable system may now reach up to 36.7% of all cable subscribers nationwide.<sup>81/</sup> As Dr. Katz concludes in the supplemental comparative analysis of the revised cable horizontal and national broadcast ownership limits, the new cable rules "allow for a much greater degree of concentration than does the broadcast television national multiple ownership rule."<sup>82/</sup> Dr. Katz concludes that the Commission's determination that "allowing increased concentration of cable system ownership is in the public interest" represents "one more piece of evidence that it is in the public interest to abolish or substantially relax the broadcast television national multiple ownership rule."<sup>83/</sup>

In the Cable Horizontal Ownership Order, the Commission determined that the measurement of a cable MSO's horizontal reach should be based upon that ratio of the MSO's subscribership to

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<sup>80/</sup> Cable Horizontal Ownership Review Order at ¶ 1.

<sup>81/</sup> Id. at ¶ 6.

<sup>82/</sup> Michael L. Katz, "A Comparative Analysis of the Broadcast Television National Multiple Ownership Rule and Cable Horizontal Ownership Rules," November 1999 ("Katz Comparative Analysis") (attached as Exhibit 1) at 2.

<sup>83/</sup> Id.

the total number of subscribers nationwide rather than a ratio of the homes passed by the MSO to the total cable homes nationwide. This change was based upon the view that a subscriber-based standard represented a more accurate gauge of market power, than a homes-passed standard.<sup>84/</sup> In effect, the Commission recognized that the number of homes actually being served by a cable operator more accurately reflects its market impact than its potential viewership.

In the broadcast context, however, a station owner's potential audience continues to be the yardstick for measuring its horizontal reach regardless of its actual share of the viewing audience. In the Order, the Commission expressly noted this difference, observing that

In contrast to the cable rules, the broadcast rules apply to single channel facilities where there are generally numerous directly competitive broadcast outlets in the market. Because a broadcast station competes with other broadcast stations in a local market and viewers therefore have several options for television viewing, a broadcast station owner does not actually have 100% of the local market's viewers all of the time. Thus, a broadcast station owner at the 35% national ownership limit cannot be deemed to have 35% of the nation's broadcast television viewers all of the time.<sup>85/</sup>

While the Commission is correct to observe that, in contrast to cable operators, a broadcaster's actual audience reach falls well short of its potential viewership due to competition, its regulatory framework more stringently limits a broadcaster's national reach. Thus, as Dr. Katz points out, "the application of approximately 'equal' limits to broadcast and cable ownership" far more severely restricts broadcast owners.<sup>86/</sup> Even though similar numerical limits may be applied to cable operators and broadcasters, the level of viewership of a single cable system's offerings versus a single broadcaster's offerings inevitably differs.

Based upon recent viewership trends, a network broadcast station can expect, at best, to be viewed by less than 15% of the homes in a given market on average throughout any given day, due

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<sup>84/</sup> Cable Horizontal Ownership Review Order at ¶ 22.

<sup>85/</sup> Id. at ¶ 64.

<sup>86/</sup> Katz Comparative Analysis at 3.

to competition from other stations and cable networks.<sup>87/</sup> Thus, even though a strong broadcaster is being viewed on a given day in less than one out of seven homes it passes in a particular market, all of the homes in that market are counted against its 35% national limit.<sup>88/</sup> By contrast, even though a cable operator, on average, serves two out of every three homes passed,<sup>89/</sup> its national reach is now measured only by reference to its actual level of subscribership.

The upshot is that the Commission's adoption of a subscriber-based limitation on a cable operator's national reach are more tailored to the number of revenue-producing homes served by that operator than is the case for broadcasters. A broadcaster's national reach is measured on the basis of all the homes it passes, notwithstanding the fact that its principal source of revenue -- advertising -- is derived only from the number of homes actually tuned in. Thus, while a cable operator's ability to expand is limited only by the number of its revenue-producing homes, a broadcaster's capacity to grow is constrained by a large number of non-revenue producing homes.

In comparing the revised cable ownership rules with the national broadcast ownership rule at issue here, Dr. Katz notes that the Commission's liberalization of the cable rules occurred despite the fact that cable viewing markets are much more concentrated than broadcast viewing markets.<sup>90/</sup>

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<sup>87/</sup> See Katz at Figure 4 (noting that average day household rating of all broadcast stations combined in 1999 is projected to be 17.1); "Basic Cable Viewership for Just-Completed 1998/99 Season Reaches Record Heights," [www.cabletvadbbureau.com/news/092199news.htm](http://www.cabletvadbbureau.com/news/092199news.htm). (noting average day household rating of broadcast network affiliates fell to 14.1 percent in 1998/99 season).

<sup>88/</sup> Even if only primetime hours are considered, a single broadcasters still can expect to be seen in fewer than 1 in 4 homes they pass. *Id.* (noting that 4 networks average primetime rating last season was a combined 30%). See also Katz Comparative Analysis at Table I (noting that the average prime time share of television households enjoyed by the top broadcaster in the first, twenty-fifth and fiftieth markets in the country was 10.4, 11.3 and 12 respectively).

<sup>89/</sup> See In the Matter of Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming, CS Docket No. 98-102, Fifth Annual Report, FCC 98-335 (released December 23, 1998) at ¶¶ 16-17 (reporting that cable systems served 65.4 million of 95.1 million homes passed -- or 68.7 percent -- in June of 1998).

<sup>90/</sup> Katz Comparative Analysis at 4-7.

Since viewing takes place at a local level, the relevant markets for assessing the effects of concentration on viewer choice and the ability of a distributor to exercise bottleneck control also are local.<sup>91/</sup> More than half of all local television markets have seven or more television stations. And because markets with larger populations tend to be the ones with greater numbers of stations, the majority of television households are located in markets with 11 or more stations.<sup>92/</sup> The vast majority of local markets have only one cable system, which is subject to some competition from DBS.<sup>93/</sup>

As Dr. Katz notes, the differences in concentration can be summarized by calculating market shares and the resulting Herfindahl-Hirschman indexes for local markets in cable and broadcast television. For purposes of illustration, these calculations adopt the Commission's position that the relevant product markets are multichannel video-programming distribution and broadcast television respectively. Using national data from the Commission to construct a representative local market, an average cable system had a market share of over 85 percent in June 1998 and an estimated HHI was 7,015. As the Commission itself noted, this is far above the threshold used by the U.S. Department of Justice and the Federal Trade Commission to determine that a market is highly concentrated.<sup>94/</sup> As Dr. Katz observes, "no broadcast station comes close to having an 85 percent market share."<sup>95/</sup> Thus, while one can debate whether even a cable system constitutes a bottleneck asset, there is no question that a single broadcast television station does not.

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<sup>91/</sup> Id. at 5.

<sup>92/</sup> Warren Publishing, Inc., Television and Cable Factbook, Stations Volume No. 67, 1999 Edition, "Affiliations by Market," C-48--C-51.

<sup>93/</sup> Katz Comparative Analysis at 5.

<sup>94/</sup> Katz Comparative Analysis at 6-7; In the Matter of Annual Assessment of the Status of Competition in the Markets for the Delivery of Video Programming, Fifth Annual Report, CS Docket No. 98-102 (released Dec. 23, 1998) at ¶128.

<sup>95/</sup> Katz Comparative Analysis at 7, ¶ 17.

Even assuming *arguendo* that national ownership has some relevance for program production markets, it is clear that a single broadcaster has no ability to exercise monopsony power or bottleneck control.<sup>96/</sup> For example, if a single entity owned a cable system in each market, that company would own approximately 85 percent of the total multichannel distribution capacity nationwide.<sup>97/</sup> By contrast, even if one company owned one television station in each market, it would control less than nine percent of the total broadcast transmission capacity (as measured by broadcast channels times total number of television households). If a company owned one television station in every market with eight or fewer stations and owned two stations in every market with nine or more stations (as could be allowed under the local ownership rules), it still would own less than 14 percent of total broadcast distribution capacity.<sup>98/</sup> Thus, as Dr. Katz notes, even though “concentrated ownership of cable systems is a much greater threat to program producers” than allowing a single broadcaster to attain a broad national reach, broadcasters are subject to more stringent national ownership restrictions than cable operators under the Commission’s present regulatory framework.<sup>99/</sup>

Finally, in the Cable Horizontal Ownership Order, the Commission revised the cable horizontal rules to explicitly take account of the competition faced by cable operators from DBS, MMDS, and other competing providers of multichannel video programming service (MVPDs). The new rules include DBS, MMDS and other customers of competing MVPDs in the total subscribership “denominator” against which the 30% limit is measured.<sup>100/</sup> The change in the

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<sup>96/</sup> Id. at 8-14.

<sup>97/</sup> Id. at 14, ¶28.

<sup>98/</sup> Id. at 14, ¶ 27. Of course, this figure itself is conservative since it does not take into account the scores of cable channels available as distribution outlets for program producers. Thus, a broadcaster’s share of total program distribution capacity is even lower than the figures set forth here and in the Katz comparative analysis.

<sup>99/</sup> Katz Comparative Analysis at 12-14.

<sup>100/</sup> Cable Horizontal Ownership at ¶ 37.

denominator results in “a significant relaxation of the rule” by increasing the horizontal limits on cable system ownership.

Perhaps more importantly, this rule change allows cable operators to adapt and respond to competition by entering new markets. As customers are siphoned away from cable operators due to competition, the new rules preserve an operator’s ability to maintain its level of subscribership (and revenues) by expanding into new markets. By contrast, apart from the Biennial Review process, no such adjustment mechanism has ever been present with respect to the broadcast rules, even though broadcasters have been facing more intensive competition for a longer period of time than have cable operators.

As with the relaxation of the duopoly rule, the Commission’s modifications to the cable horizontal ownership rules make it far more difficult to justify continued retention of the national limits on broadcast station ownership -- particularly in their present form. Having moved to an actual viewership yardstick in the cable context, fashioned rules that explicitly take account of the competition faced by operators, and provided cable with the opportunity to expand into new markets as it loses market share to competitors, there is little justification for, at a minimum, failing to undertake similar efforts in the broadcast context.

## **CONCLUSION**

Congress has specifically and explicitly directed the Commission to reconsider its broadcast ownership rules every two years, and to eliminate regulations rendered obsolete by competition. Whatever justification that once might have existed for the national limits on broadcast station ownership has long since evaporated, and their anachronistic status in the marketplace becomes clearer with each passing day and with each new decision the Commission reaches. Accordingly, the

Commission should move immediately to eliminate the national audience reach cap on TV station ownership.<sup>101/</sup>

Respectfully submitted,

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<sup>101/</sup> Fox continues to adhere to the view set forth in its initial comments that if any ownership cap is retained, the UHF discount reflects and remedies technical and competitive impediments faced by UHF broadcasters and therefore should not be altered or modified.

**A COMPARATIVE ANALYSIS OF THE BROADCAST  
TELEVISION NATIONAL MULTIPLE OWNERSHIP RULE  
AND CABLE HORIZONTAL OWNERSHIP RULES**

**Michael L. Katz**

**18 November 1999**

## I. INTRODUCTION AND QUALIFICATIONS

1. My name is Michael L. Katz, and I declare as follows. I am the Edward J. and Mollie Arnold Professor of Business Administration at the University of California at Berkeley. I hold a joint appointment in the Haas School of Business Administration and the Department of Economics. I serve as Director of the Center for Telecommunications and Digital Convergence at the University of California at Berkeley. I have also served on the faculty of the Department of Economics at Princeton University. I received my A.B. from Harvard University *summa cum laude* and my doctorate from Oxford University. Both degrees are in Economics.

2. I specialize in the economics of industrial organization, which includes the study of antitrust and regulatory policies. I regularly teach courses on microeconomics, business strategy, and telecommunications policy. I am the author of a microeconomics textbook, and I have published numerous articles in academic journals and books. I have written articles on several issues, including network effects, antitrust policy enforcement, and telecommunications policy. Exhibit A lists all publications that I have authored or co-authored, with the exception of a few letters to the editor on telecommunications policy. I am a coeditor of the *Journal of Economics & Management Strategy*, and I serve on the editorial board of the *California Management Review*.

3. In addition to my academic experience, I have consulted on the application of economic analysis to issues of antitrust and regulatory policy. I have served as a consultant to both the U.S. Department of Justice and the Federal Communications Commission ("the Commission") on issues of antitrust and regulatory policy in telecommunications markets. I have served as an expert witness before state and federal courts, and I have provided expert testimony before a state regulatory commission as well as Congress. In 1994 and 1995, I served as Chief Economist

of the Commission. Since leaving the Commission, I have appeared before it at several public forums.

4. I have been asked by counsel for Fox Television Stations, Inc. to analyze the relationship between the rules governing national multiple ownership of broadcast television stations and the rules governing national multiple ownership of cable television systems. Drawing on my training and experience as an economist, my review of the facts, and my knowledge of the broadcasting and cable television industries, I find the following:

- Superficially, the broadcast television national multiple ownership rule and the cable horizontal ownership rules are similar. But, in fact, the rules use very different bases for calculating whether an owner exceeds the relevant cap.
- The industries to which the rules apply also are very different. A typical cable system has much greater *absolute* programming capacity and accounts for a much greater *share* of viewers and capacity in its local area than does a television station.
- Because of the differences both in how ownership is calculated and in the underlying industries, application of the superficially similar rules leads to very different effects in practice: The cable horizontal ownership rules allow for a much greater degree of concentration than does the broadcast television national multiple ownership rule.
- Under the current rules, cable ownership is much more concentrated at the national level than is broadcast ownership. By any reasonable measure, national ownership of broadcast television stations is highly fragmented and is not concentrated. Sinclair Broadcast Group, Inc.—the largest group owner measured in terms of the number of television stations controlled—owns fewer than five percent of U.S. commercial television stations. Fox Television Stations, Inc.—the largest broadcast television group owner measured by national reach—owns stations that on average are viewed by less than three percent of U.S. television households. Similarly, Fox owned and operated stations accounted for less than four percent of national broadcast television capacity for reaching viewers.
- The Commission recently found that allowing increased concentration of cable system ownership is in the public interest. This finding is one more piece of evidence that it is in the public interest to abolish or substantially relax the broadcast television national multiple ownership rule.

The remainder of this declaration explains the factual and logical analysis that leads to these conclusions.

## II. BACKGROUND

5. Both cable multiple systems operators (“MSOs”) and broadcast television station group owners are subject to national ownership limits. Broadcast television ownership is governed by the national multiple ownership rule, under which a single entity cannot control stations whose combined reach exceeds 35 percent of U.S. television households.<sup>1</sup> Cable television ownership is governed by the cable horizontal ownership rules, under which no cable operator can control systems serving more than 30 percent of all multichannel video-programming subscribers nationwide.<sup>2</sup> The Commission has found that this is effectively a 36.7 percent cap on U.S. cable households.<sup>3</sup>

6. On the surface, the broadcast and cable rules are similar. In each case, the ownership cap is intended to prevent a single owner from acting as a media gatekeeper by exercising market power as a buyer (so-called monopsony power) or by limiting viewer options.<sup>4</sup> And in each case, a single owner is not allowed to control distribution systems covering more than about a third of the households reached by the respective industries.

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<sup>1</sup> 47 CFR § 73.3555(e). When a group owner holds two licenses within a single Designated Market Area, that audience is counted only once for purposes of the national reach cap. See *In the Matter of Broadcast Television National Ownership Rules, Review of the Commission’s Regulations Governing Television Broadcasting, and Television Satellite Stations Review of Policy and Rules*, Report and Order, released August 6, 1999, ¶ 1.

<sup>2</sup> 47 CFR § 76.503.

<sup>3</sup> See *In the Matter of Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992 and Horizontal Ownership Limits*, Third Report and Order, MM Docket No. 92-264 (“*Horizontal Ownership Third Report and Order*”), released October 20, 1999, ¶ 6.

<sup>4</sup> For a summary of the rationale for the cable horizontal ownership rules see *Horizontal Ownership Third Report and Order*, ¶¶ 13-14. Proponents of the broadcast television national cap argue that it protects the public interest in several dimensions, including: (a) competition; (b) diversity; (c) minority ownership; and (d) localism. It is notable that promoting minority ownership and localism were not originally stated as rationales for the adoption of the national multiple ownership cap. See *In the Matter of Amendment of Section 73.3555 [formerly Sections 73.35, 73.240, and 73.636] of the Commission’s Rules Relating to Multiple Ownership of AM, FM, and Television Broadcast Stations*, Report and Order, released August 3, 1984, ¶ 17.

7. While they set similar numerical limits, the broadcasting and cable television ownership rules are in fact very different. A critical difference arises in how an owner's national share is calculated. Under the cable horizontal ownership rules, only actual cable subscribers—not all homes passed—are included in the calculation of whether an MSO meets the ownership cap. Under the broadcast television national multiple ownership cap, however, all homes reached or "passed" are counted against the cap. As the data discussed below will make clear, this distinction is an extremely significant one.

8. Moreover, because they apply to such dissimilar industries, even if the rules were the same, their effects would be very different. A typical television viewer can be reached through only one cable system, and that system offers scores of channels. In contrast, a typical television viewer can choose among several broadcast stations, each of which offers only one channel of programming. Consequently, even if a broadcast station owner controlled stations with 100 percent national reach, that owner would not be able to restrict the supply of independent programming to viewers or exercise significant monopsony power in the purchase of programming—there would be too many alternative outlets through which programmers and viewers could reach one another.

9. Both because the rules are not really equal, and because the industries to which they apply are dissimilar, the application of apparently equal limits to broadcast and cable television ownership allows much greater concentration in cable television than in broadcast television. The next section documents the differences between broadcast and cable television in greater detail and examines the implications for ownership concentration.

### **III. THE BROADCAST TELEVISION AND CABLE TELEVISION INDUSTRIES ARE VERY DIFFERENT**

10. There are a number of differences between the broadcast and cable television industries. All of these differences indicate that concentrated national ownership raises greater competitive issues in the cable industry than in the broadcast television industry.

#### **A. Cable Viewing Markets are Much More Concentrated than are Broadcast Viewing Markets**

11. One of the important differences between the two industries is in the concentration of ownership. In order to determine the degree of ownership concentration, one must define the relevant markets. Once these markets have been defined, it is possible to calculate market shares if sufficient data are available. The calculated market shares often are used to provide an indication of the presence or absence of market power, although it is widely recognized that several other factors must be taken into account as well.

12. Relevant markets are defined along two dimensions: the scope of the products included and the geographic scope. A fundamental principle by which economists define the product scope of a market is to include two goods or services in the same relevant market if consumers view them as sufficiently close substitutes, and not include them in the same relevant market if consumers do not view them as substitutes.<sup>5</sup> Similarly, the central approach to geographic market definition is to include products available at two locations in the same relevant market if they are viewed by consumers as being substitutes for one another, and to place them in separate markets if consumers do not view them as substitutes.<sup>6</sup>

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<sup>5</sup> See, for example, U.S. Department of Justice and the Federal Trade Commission, *Horizontal Merger Guidelines*, April 2, 1992 (revised April 8, 1997) ("Merger Guidelines") § 1.11, and *In the Applications of NYNEX Corporation Transferor, and Bell Atlantic Corporation Transferee, For Consent to Transfer Control of NYNEX Corporation and Its Subsidiaries*, Memorandum Opinion and Order, FCC 97-286 ("NYNEX-Bell Atlantic Order"), released August 14, 1997, ¶ 50.

<sup>6</sup> See *Merger Guidelines*, § 1.2, and *NYNEX-Bell Atlantic Order*, ¶ 50.

13. In terms of product scope, the Commission apparently considers broadcast television and multi-channel video programming distribution ("MVPD") to be separate and distinct relevant markets, for at least some purposes.<sup>7</sup> It is evident that the relevant product markets are no narrower than broadcast television and MVPD. There are good reasons to conclude that the product scope relevant for the analysis of the broadcast television national multiple ownership cap is broader than broadcast television.<sup>8</sup> Rather than debate the appropriate scope of product markets here, however, I will examine concentration of broadcast television and MVPD "markets." By taking a narrow approach to product market definition, I am erring on the side of overstating the degree of concentration and resulting competitive concerns.

14. Now, consider the geographic boundaries of relevant markets. As the Commission has long recognized, the single most important fact in analyzing the effects of ownership concentration on viewers and advertisers is that viewing takes place at a local level.<sup>9</sup> This fact implies that the relevant markets for assessing the effects of concentration on viewer choice are local.

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<sup>7</sup> In particular, the cable horizontal ownership limit is based on MVPD *subscribers* and thus appears to exclude broadcast television from consideration (*Horizontal Ownership Third Report and Order*, ¶ 5). In its annual assessment of competition in the delivery of video programming, the Commission identifies broadcasters as participants in the MVPD market, but then broadcasters are excluded as market participants in the calculations of market concentration. See *In the Matter of Annual Assessment of the Status of Competition in the Markets for the Delivery of Video Programming*, Fifth Annual Report ("Video Competition Report"), released December 23, 1998, ¶¶ 95 and 128. The extent to which the Commission considers cable television channels to compete with broadcast television is even more difficult to discern.

<sup>8</sup> For an overview of how cable and direct-to-the-home satellite television channels compete with broadcast television for viewers and advertising, see Michael L. Katz, "Old Rules and New Rivals: An Examination of Broadcast Television Regulation and Competition" ("Katz White Paper"), September 1999, at 52-82, submitted as an attachment to "Supplemental Comments of Fox Television Stations, Inc.," *In the Matter of 1998 Biennial Regulatory Review—Review of the Commission's Broadcast Ownership Rules and Other Rules Adopted Pursuant to Section 202 of the Telecommunications Act of 1996*, submitted 18 November 1999.

<sup>9</sup> See, for example, *In the Matter of Amendment of Section 73.3555 [formerly Sections 73.35, 73.240, and 73.636] of the Commission's Rules Relating to Multiple Ownership of AM, FM, and Television Broadcast Stations*, Report and Order, released August 3, 1984, ¶¶ 10 and 31.

15. An examination of the data clearly demonstrates that local MVPD markets are far more concentrated than are local broadcast television markets. The vast majority of local markets have only one cable system. Direct-to-the-home satellite television provides competition, but it is limited by lack of local channels.<sup>10</sup> The situation in broadcast television is very different. More than half of all television markets have seven or more television stations.<sup>11</sup> And because markets with larger populations tend to be the ones with greater numbers of stations, the majority of television households are located in markets with 11 or more stations.<sup>12</sup>

16. The differences in concentration can be summarized by calculating market shares and the resulting Herfindahl-Hirschman indexes (HHIs) for local markets in cable and broadcast television.<sup>13</sup> The Commission, the Federal Trade Commission, and the U.S. Department of Justice all use the HHI as a measure of concentration and a rough tool for identifying markets in which the size and number of suppliers may raise competitive concerns.<sup>14</sup> Using national data to construct a representative local market, the Commission found that an average cable system had a market share of over 85 percent in June 1998 and the estimated HHI was 7,015.<sup>15</sup> As the Commission itself noted, this is far above the threshold used by the U.S. Department of Justice and the Federal Trade Commission to determine that a market is highly concentrated.

17. No broadcast station comes close to having an 85 percent market share. Table 1 illustrates the prime time shares of the affiliates of leading stations in three markets.

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<sup>10</sup> *Video Competition Report*, ¶ 63. This disadvantage is expected to diminish as the result of legislation.

<sup>11</sup> Warren Publishing, Inc., *Television & Cable Factbook*, Stations Volume No. 67, 1999 Edition, "Affiliations by Market," C-48 – C-51.

<sup>12</sup> Warren Publishing, Inc., *Television & Cable Factbook*, Stations Volume No. 67, 1999 Edition, "Affiliations by Market," C-48 – C-51.

<sup>13</sup> The HHI for a market is calculated by summing the squared market shares of the sellers in that market.

<sup>14</sup> See, for example, *Video Competition Report*, ¶ 127, particularly footnote 562.

<sup>15</sup> *Video Competition Report*, ¶ 128. According the Commission, cable's market share fell to 82 percent by June 1999 (*Horizontal Ownership Third Report and Order*, ¶ 29, typographical error in original).